Supreme Court, U. S.
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IN THE

Supreme Court of the United States

October Term, 1976

No. 76-908

THE CITIZENS AND SOUTHERN NATIONAL BANK,
Petitioner

v.

UNITED STATES OF AMERICA,
Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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The Citizens and Southern National Bank, petitioner herein, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit entered in case No. 75-2549 on September 15, 1976, on appeal from the District Court for the Southern District of Georgia. Petition for rehearing was denied on November 16, 1976.

The judgment also dealt with case No. 75-3571 on appeal from the District Court for the Middle District of Georgia. A separate petition for the writ will be filed in that case.

OPINION BELOW

The opinion of the court below (Appendix p. 1a) is reported at 538 F.2d 1101 (5th Cir. 1976). It reversed the judgment of the District Court for the Southern District of Georgia (Appendix p. 21a), and remanded the case for the entry of judgment in favor of the United States.

JURISDICTION

The judgment of the court below was entered September 15, 1976. Petition for rehearing was denied on November 16, 1976 (Appendix p. 19a). Mandate was stayed to and including January 3, 1977. Jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

1. Whether the court of appeals erred in holding that under Georgia law petitioner was in possession of

"property" or "rights to property" belonging to Robert W. Best, a customer, subject to levy under Sections 6331 and 6332 of the Internal Revenue Code to enforce a tax lien asserted against Best under Section 6321 of the Internal Revenue Code where, prior to assessment of the tax and prior to the date of the notice of levy, Best had assigned and conveyed to petitioner all of his balances, credits, deposits and accounts as security for the payment of indebtedness owed by him to petitioner, which indebtedness at the time of the notice of levy exceeded the amount of the assigned balances, credits and accounts.

2. Whether in view of the Georgia statute providing that all choses in action arising upon contract may be assigned so as to vest title in the assignee, the court of appeals erred in holding that the choses in action into which the funds deposited by Best had been transformed were subject to levy as "property" or "rights to property" belonging to Best after such choses in action had been assigned by Best to petitioner as collateral.

3. Whether the court of appeals erred in holding that the assignments from Best to petitioner of the choses in action representing his deposit account were "written to operate in the future", or whether such assignments had the effect under Georgia law of vesting legal title to the same in petitioner as of the dates of the respective assignments to the extent of the amount of the secured indebtedness.

4. Whether the United States has any greater rights than the taxpayer with respect to third parties and the contractual relation existing between them for the purpose of enforcing a tax lien asserted under Section 6321 of the Internal Revenue Code.

5. Whether the court of appeals erred in failing to hold

the tax lien here involved invalid pursuant to Section 6323(a) and (h) (1) as against the assignments held by petitioner covering the choses in action sought to be levied upon.

STATUTES INVOLVED

Internal Revenue Code of 1954 (26 U.S.C.):

Sec. 6321 which creates a lien upon all property and rights to property of a delinquent taxpayer.

Sec. 6323 (a) (h) (1) which provides that such lien shall not be valid as against any purchaser or holder of a security interest, and defining a security interest.

Sec. 6331 which provides for levy of the tax lien.

Sec. 6332 which requires the surrender by a person in possession of property or rights to property belonging to the taxpayer and subject to levy.

Georgia Code Ann. § 85-1803 relating to assignment of choses in action arising upon contract so as to vest title in the assignee.

Appendix pp. 31a - 33a.

STATEMENT OF THE CASE

Robert W. Best was a depositor and loan customer of petitioner, borrowing money from time to time and executing to petitioner promissory notes, each containing the following language:

> "To secure the payment of this Note and all other indebtedness or liabilities of the undersigned

> to Holder, however and whenever incurred or evidenced, whether direct or indirect, absolute or contingent, or due or to become due (hereafter with this Note, collectively called 'Liabilities'), undersigned transfers and conveys to Holder any and all balances, credits, deposits, accounts, items and monies of the undersigned now or hereafter with the Holder, and the undersigned agrees that the Holder shall have a lien upon, security title to and a security interest in all property of the undersigned of every kind and description now or hereafter in the possession or control of the Holder for any reason. . . ."

The notes held by petitioner on the date pertinent here were dated February 19, 1973, February 20, 1973, March 26, 1973, and April 18, 1973, respectively. Some notes were those of Best alone and others were signed by Best and a co-maker. Two other notes dated November 7, 1972, and March 28, 1973, respectively, had been guaranteed by Best. These latter notes also contained the language quoted above.

On May 2, 1973, the Government made a tax assessment against Best for unpaid wagering excise taxes in the amount of $741,093.49. Best failed and refused payment upon demand. Notice of tax liens were then filed.

On May 3, 1973, an Internal Revenue Service agent served a notice of levy upon petitioner, demanding that it surrender and remit all property, rights to property, monies, credits and bank deposits in its possession belonging to Best.

At the time of service of the notice of levy, Best had a checking account reflecting a balance of $57,365.58. At

the same time, Best owed petitioner an amount in excess of $60,000.00 upon the promissory notes executed by himself alone, or by himself and a co-maker, and upon which Best was jointly and severally liable.

Following such notice of levy, petitioner in accordance with the provisions of such promissory notes, applied the amount in said checking account toward payment of Best's indebtedness to it and on May 4, 1973, Best was notified by letter to that effect.

After such application, Best remained indebted to petitioner. Accordingly, petitioner responded to the demand of the Internal Revenue Service to the effect that it had no property belonging to Best in its possession and that it was not indebted to Best.

Thereafter on May 16, 1974, this suit was filed seeking judgment against petitioner for the sum of $57,365.58, representing the amount alleged in the complaint to have been owing by petitioner to Best at the time of the notice of levy. Petitioner's answer to the complaint included a denial that it was possessed of any property or rights to property belonging to Best which were subject to levy at the time of the service of notice. The answer averred that since the indebtedness of Best to petitioner was greater than that of petitioner to Best, there was no net indebtedness owing by petitioner to Best subject to levy.

The case proceeded to trial upon stipulation of the undisputed facts and the exhibits thereto attached. On April 21, 1975, judgment was entered in favor of petitioner. (Appendix p. 21a). The court construed the pertinent provision contained in each promissory note of Best pursuant to the applicable law as follows:

"Under Georgia law, this clause constituted an

assignment of Best's chose in action as collateral security for the debts evidenced by those promissory notes and operated as a valid assignment of all Best's rights as creditor of the Bank, existing by reason of his deposits, until the notes were paid. **See Macon National Bank v. Smith,** 170 Ga. 332, 338 (1930). Thus C & S was not in possession of property or rights to property of the taxpayer at the time it received notice of the tax levy. For this reason, it cannot be held liable under section 6332(c) for its failure to turn over the funds deposited in Best's account." (Appendix p. 28a).

On appeal the court of appeals reversed such judgment on September 15, 1976, and remanded the case for the entry of a judgment for the government. (Appendix p. 17a) A motion for rehearing was filed and denied on November 16, 1976. (Appendix p. 19a).

REASONS FOR GRANTING THE WRIT

1. The petition raises substantial and important questions relating to the enforcement of federal tax liens in that the judgment sought to be reviewed contravenes applicable Georgia law defining property and property rights subject to levy.

2. To review a judgment which does not follow the principle laid down by this Court in ACQUILINO v. UNITED STATES, 363 U. S. 509 (1960), that both federal and state courts must look to state law to determine the question of whether there exist property or rights to property belonging to a taxpayer and subject to levy.

3. To review a judgment which purports to follow the law of Georgia but which, in reality, was based upon or influenced by holdings from other jurisdictions where the

state law there involved is substantially different than that of Georgia, or where a state had no definitive law on the subject.

4. To review the judgment herein so as to preserve the integrity of state law in an area specifically recognized by this Court to be solely within the province of the states from modification or misapplication by the federal judiciary, and in order to maintain the proper balance between the state and federal governments which is vital to our federalism.

ARGUMENT

PETITIONER DID NOT HAVE IN ITS POSSESSION AT THE TIME THE NOTICE OF LEVY WAS SERVED ANY "PROPERTY" OR "RIGHTS TO PROPERTY" BELONGING TO ROBERT W. BEST AND SUBJECT TO LEVY.

This question is resolved by resort to the applicable law of Georgia. In ACQUILINO v. UNITED STATES, 363 U. S. 509, 80 S.C. 1277, 4 L.Ed. (2) 1365 (1960), this Court held:

> "The threshold question in this case, as in all cases where the federal Government asserts its tax lien, is whether and to what extent the taxpayer had 'property' or 'rights to property' to which the tax lien could attach. In answering that question both federal and state courts must look to state law, for it has long been the rule that 'in the application of a federal revenue act, state law controls in determining the nature of the legal interest which the taxpayer had in the property sought to be reached by the statute.' "

While recognizing that State law controls in this area, nevertheless, the court of appeals overlooked or disregarded a controlling Georgia statute and misconstrued and misapplied decisions of the Supreme Court of Georgia construing and applying that statute.

Section 85-1803 of the Code of Georgia provides:

> "All choses in action arising upon contract may be assigned so as to vest the title in the assignee, but he takes it, except negotiable instruments, subject to the equities existing between the assignor and debtor at the time of the assignment, and until notice of the assignment is given to the person liable."

That statute (Section 3653, Code of Georgia of 1910) was cited and applied in MACON NATIONAL BANK v. SMITH, 170 Ga. 332, 337 (153 S. E. 4). The pertinent portion of that decision is as follows:

> "Another principle of law is that all choses in action arising upon contract may be assigned in writing so as to vest the title in the assignee. Civil Code, § 3653; [citing cases]. . . . The note of General Sprayer Company to the Macon National Bank contained the clause: 'Each of us further agrees that any and all deposits due by said bank to either of us may at all times be considered by said Bank as collateral to this loan, and may be applied at any time by said bank in whole or part payment of this loan.' This was a sufficient assignment of the chose in action as collateral security for the debt evidenced by the note. It was a good assignment as collateral security of all right of the company as creditor of the bank, existing by reason of the deposit account, as it was and as it may appear on

the books of the bank, from day to day and 'at all times' until the note shall be paid. The interest of the bank as transferee of the deposit account vested at the date of the note, October 22, 1927, prior to summons of garnishment on December 8, 1927, and therefore was entitled to preference, as against Smith, the garnishing creditor, relatively to the amount on deposit ($1456.64) on the date of service of the summons of garnishment. It may be remarked that the garnishing creditor did not acquire a better status with reference to this fund as against the bank than the company occupied. Upon this point see HAAS v. OLD NATIONAL BANK, 91 Ga. 307 (18 S. E. 188); FIDELITY & DEPOSIT CO. v. EXCHANGE BANK, 100 Ga. 619 (28 S. E. 393)."

See also SPROUSE v. SKINNER, 155 Ga. 119, 122 (116 S. E. 606), and SAUL v. BOWERS, 115 Ga. 450 (117 S. E. 86) where the rule was also applied to the transfer of choses in action assigned as collateral.

The statute has been similarly applied with respect to the assignment of a life insurance policy. In PARRAMORE v. WILLIAMS, 215 Ga. 179, 180 (109 S. E. 2d 745), it was held:

> "A policy of life insurance is a chose in action and may be assigned by the insured as security for a debt, under Code §§ 28-301, 56-903, and 85-1803, and generally the effect of such an assignment is to vest legal title to the policy in the assignee to the amount of the debt secured."

Thus, after the execution of the assignments, the choses in action here involved belonged to petitioner and not the taxpayer. No right to property existed or could

accrue in favor of the taxpayer with respect to the assigned accounts unless and until the amount of such account exceeds the amount of the secured indebtedness. That did not occur.

In UNITED STATES v. BANK OF SHELBY, 68 F.2d 538 (5th Cir. 1934), a Mississippi case, the court held that where a depositor owed a bank more than the bank owed the depositor, there was at the time of levy no property or right to property of the taxpayer which the taxpayer could assert and, consequently, nothing upon which to levy. The court of appeals in its opinion in the instant case attempted to distinguish BANK OF SHELBY on the basis that the depositor there was insolvent. But that is not a distinguishing criterion, for the underlying rationale of BANK OF SHELBY is equally applicable here, the court stating at 68 F.2d 538, 540:

> "In the case before us the bank could either at law or in equity have defeated a demand by Toler [the taxpayer/depositor] for payment on June 17, 1925 [date of notice of levy], of the money apparently to his credit by offsetting the note which produced the credit, and the United States can only claim under and through him and subject to the defenses and equities affecting him."

The principle decided in MACON NATIONAL BANK v. SMITH, supra, was followed and that case cited in GEORGIA BANK & TRUST CO. v. HADARITS, 221 Ga. 125, (143 S. E. 2nd 627). In the latter case, the Supreme Court of Georgia granted certiorari to review a decision by the Court of Appeals of Georgia which did not follow MACON NATIONAL BANK.

After reciting its reasons for granting the writ, [1] the court held:

> "With this firm right to such deposits thus fixed, waiver by the bank in favor of any number of checks drawn against the account would in nowise affect or nullify its positive right to such accounts at such time as it freely elected to do so. No holder of a check by the depositor had a right to have it paid in preference to the bank's claim, or to complain because the bank paid other checks drawn thereon. In all such transactions the bank could hurt only itself, and those holding checks that the bank refused to pay in preference to itself have no standing to complain since no right of theirs is violated. They are not occupying a position of innocent purchaser. Their checks are good only to the extent that there are on deposit funds available for the purpose of paying the same." Id. at 126.

In STUART v. WILLIS, 244 F.2d 925 (9th Cir. 1957), the court stated at 929:

> "In fact, it may be generally stated as a principle of our federal tax law that the power of the Collector never extends beyond the rights of the taxpayer upon whose property the levy is sought."

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[1] "The writ of certiorari was issued to the Court of Appeals in GEORGIA BANK & TRUST CO. v. HADARITS, 111 Ga. App. 195 (141 SE2d 172), which held that a bank, although it had the right to apply a depositor's account to the payment of a note under an assignment of the account to the bank as collateral security, and had

The underlying rationale is also expressed in UNITED STATES v. WINNETT, 165 F.2d 149 (9th Cir. 1947), where the court observed that:

> ". . . the rights of the collector (of Internal Revenue) do not extend beyond those of the taxpayers whose right to property is sought to be levied upon."

The judgment in question should be reviewed because the court of appeals obviously failed to follow the guidelines laid down by this Court in ACQUILINO v. UNITED STATES, supra, in determing the threshold question. After quoting from that decision, the court of appeals ironically overlooked or disregarded entirely the Georgia statute (Ga. Code Ann. § 85-1803) and then undertook to distinguish the decisions which enunciate and apply the well-established law of Georgia with respect to assignments of choses in action of the kind here involved. As a criterion for distinguishing MACON NATIONAL BANK and GEORGIA BANK & TRUST CO., supra, the court placed unwarranted emphasis on a single word taken from each decision. In so doing, the basic principle there decided and the substantive holdings that title vested in the assignee as of the date of the assignment and that subsequent thereto no property or rights to property remained in the assignor were overlooked or disregarded.

The cases from other jurisdictions cited in the

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1 (con't.)
paid checks drawn by the depositor which it was not obligated to pay, thus treated the account as the depositor's property and waived its right to apply the funds in the account at that time on its note . . . The applicant likewise insists that the opinion and judgment of the Court of Appeals is not in accord with a decision of this court in MACON NAT. BANK v. SMITH, 170 Ga. 332 (153 SE 4), unequivocally holding

judgment sought to be reviewed do not deal with or shed any light upon Georgia law. In UNITED STATES v. FIRST NATIONAL BANK OF ARIZONA, 348 F.Supp,. 388 (D.Ariz. 1970), the court held, contrary to the Georgia law, that until a bank has notified its depositor of exercise of the right of setoff, the depositor is free to withdraw from his account. On appeal it was held that the case was controlled by BANK OF NEVADA v. UNITED STATES, 251 F.2d 820 (9th Cir. 1958). Aside from that decision having been rendered in 1958, prior to the decision of this Court in ACQUILINO in 1960, the debt to the Bank for which the chose in action was assigned as collateral was created after the assessment of the tax lien and did not exist at the time of notice of levy.

UNITED STATES v. STERLING NATIONAL BANK & TRUST CO. OF N. Y., 494 F.2d 919 (2nd Cir. 1974), is not authority for the holding here. In that case the court plainly stated that the question of whether the Bank held property or a right to property of the taxpayer is "one of state law, in this case, New York's", (citing ACQUILINO). Also, the tax was assessed prior to the time the loan was made and the note executed. The court applied New York law and held that the "literal language of § 151 [New York Debtor and Creditor Law]. . . would indicate that the full amount in the account is the customer's property." (Id. at 922) That is in direct conflict with the Georgia law.

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1 (con't.)
that such an assignment by a debtor transferred the interest of the debtor in his account as of the date of the execution of the assignment and was effective as to each subsequent deposit by the debtor as the same was made. There are other assignments of error but the above resume is sufficient to state the case as considered by this court in the following opinion." 221 Ga. 125.

WHETHER THE TAX LIEN IS VALID PURSUANT TO SECTION 6323 (a) (h) (1) AS AGAINST THE ASSIGNMENTS HELD BY PETITIONER

If petitioner held no property or rights to property of Best at the time of the levy, then no personal judgment could be obtained against it in this suit, without regard to whether or not the tax lien was valid.

However, should it be deemed appropriate to consider the question as to the validity of the tax lien, then the assignments held by petitioner from Best must be given the legal effect accorded them by the statutory and case law of Georgia. Consequently, the validity of the tax lien must be tested by the quality of the title transferred and conveyed to the assignee. When so tested, the result is inescapable that petitioner occupies the status of a party designated in Section 6323 (a) against whom the tax lien is **not** valid.

The question here is far-reaching in importance and is calculated to be recurring.

CONCLUSION

For the reasons set forth above, it is respectfully prayed that a writ of certiorari be granted to review the judgment of the United States Court of Appeals for the Fifth Circuit in this case.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, William M. Fulcher, counsel of record for The Citizens and Southern National Bank, petitioner, and a member of the bar of the Supreme Court of the United States, hereby certify that I have served the foregoing petition for the writ of certiorari upon the United States, respondent, by depositing three copies thereof in a United States post office with first class postage prepaid addressed to Honorable Robert H. Bork, Solicitor General of the United States, Department of Justice, Washington, D.C., 20530, and one copy thereof addressed to each of the following:

Mr. Gilbert E. Andrews
Attorney, Tax Division
Department of Justice
Washington, D. C. 20530

Mr. Murray S. Horwitz
Attorney, Tax Division
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This _____ day of December, 1976.

_____
WILLIAM M. FULCHER
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APPENDIX

UNITED STATES of America,
Plaintiff-Appellant,

v.

CITIZENS AND SOUTHERN NATIONAL BANK,
Defendant-Appellee.

UNITED STATES of America,
Plaintiff-Appellant,

v.

CITIZENS AND SOUTHERN NATIONAL BANK,
Defendant-Appellee.

Nos. 75-2549, 75-3571.

United States Court of Appeals,
Fifth Circuit.

Sept. 15, 1976.

Government brought suit against banks to enforce tax levies on depositors' bank accounts. The United States District Court for the Southern District of Georgia at Augusta, Anthony A. Alaimo, J., and the United States District Court for the Middle District of Georgia at Macon, J. Robert Elliot, Chief Judge, entered judgments for banks and Government appealed. The Court of Appeals, Lively, Circuit Judge, held that under Georgia law, the existence of an indebtedness to bank exceeding the balance in a depositor's account does not divest depositor of all property and rights to property in the account; the bank's right of setoff required some discreet act by the banks, and as neither bank performed such an act until after service of notice of levy, depositors retained property interests in the accounts subject to levy.

Reversed and remanded.

1. Banks and Banking

Under Georgia law, a person who places money in a bank on general deposit loses title to the money and becomes a creditor of the bank and the funds deposited are transformed into a chose in action.

2. Internal Revenue

Even if depositors' assignments to banks of funds in accounts as security for indebtedness gave banks a contractual lien and security interest in the deposits, claim of prior lien could not be interposed as defense to action to enforce tax levy. 26 U.S.C.A. (I.R.C.1954) §§ 6321, 6331(a), 7426.

3. Banks and Banking

Under Georgia law, existence of indebtedness to banks which exceeded balance in depositors' accounts did not extinguish depositors' property interests in the account by operation of law, and as banks did not exercise rights of setoff until after levies were made for federal taxes, depositors had property interests in the accounts at time of levies. 26 U.S.C.A. (I.R.C.1954) §§ 6321, 6331(a), 7426.

4. Internal Revenue

Banks' claimed right to setoff of funds in depositors' accounts on which levies were made for federal taxes gave rise to bona fide dispute as to whether deposits represented property or rights to property of depositors, and provision for 50% penalty for failure of bank to surrender properties of taxpayer "without reasonable cause" was not applicable. 26 U.S.C.A. (I.R.C.1954) § 6332(c)(2).

Appeals from the United States District Courts for the Southern and Middle Districts of Georgia.

Before WISDOM, GODBOLD and LIVELY*, Circuit Judges.

LIVELY, Circuit Judge.

In these two cases the government appeals from judgments in favor of banks which had refused to pay to the Internal Revenue Service the balances in bank accounts upon which levies were made for federal taxes previously assessed. In each instance the bank contended that the depositor-taxpayer in whose name the account stood had no property or rights to property in the account either at the time of the assessment of taxes or the time of the levy. In each case the government brought suit to enforce the levy, and the district courts, on somewhat different reasoning, entered judgments for the banks (separate offices of Citizens and Southern).

Section 6321 of the Internal Revenue Code of 1954 (26 U.S.C. § 6321) creates a lien in favor of the United States "upon all property and rights to property, whether real or personal, belonging to . . ." a person liable for any tax who has not paid it after demand. Section 6331(a) of the Code (26 U.S.C. § 6331(a)) gives to the Secretary of the Treasury or his delegate authority "to collect such tax . . . by levy upon all property and rights to property . . . belonging to such person or on which there is a lien provided in this chapter for the payment of such tax."

The facts in both cases were stipulated. In No. 2549 the Internal Revenue Service (IRS) made an assessment for unpaid wagering excise taxes against Robert W. Best,

* Of the Sixth Circuit, sitting by designation.

a customer of Citizens and Southern National Bank (the bank), on May 2, 1973. At noon on May 3, 1973, when the checking account [1] of Best reflected a credit balance in excess of $57,000, officers of the bank determined that the bank was "insecure" with respect to indebtedness of Best to the bank in excess of $60,000 and determined to take all reasonable steps to protect the bank. At 3:05 p. m., May 3, 1973 an agent of IRS served a notice of levy directing the bank to surrender to the government the balance in the Best account. On May 4, 1973, the bank wrote Best that as of that date it had applied the balance in his account to his outstanding indebtedness to the bank. On May 8, 1973 the bank actually made the transfer entries, charging the Best account and crediting the Best notes.

Prior to the time of both the assessment and the levy Best had executed several promissory notes to the bank, each of which contained the following language:

> To secure the payment of this Note and all other indebtedness or liabilities of the undersigned to Holder, however and whenever incurred or evidenced, whether direct or indirect, absolute or contingent, or due or to become due (hereafter with this Note, collectively called "Liabilities"), undersigned transfers and conveys to Holder any and all balances, credits, deposits, accounts, items and monies of the undersigned now or hereafter with the Holder, and the undersigned agrees that the Holder shall have a lien upon, security title to and a security interest in all property of the undersigned of every kind and description now or here-

1. Best actually had several accounts but the terms of the agreement with the bank were substantially the same on all, and a single account will be referred to for convenience.

> after in the possession or control of the Holder for any reason, including all dividends and distributions on or other rights in connection therewith.
>
> In the event of nonpayment when due of any amount payable on any Liabilities, or if the Holder shall feel insecure for any reason whatsoever (1) any and all Liabilities may, at the option of Holder and without demand or notice of any kind be declared and thereupon immediately shall become due and payable, (2) the Holder may exercise from time to time any of the rights and remedies available to Holder under the Uniform Commercial Code as in effect at that time in Georgia, or otherwise available to Holder and (3) the Holder may, at any time, without demand or notice of any kind, appropriate and apply toward the payment of such Liabilities, and in such order of application as the Holder may from time to time elect, any balances, credits, deposits, accounts, items and monies of the undersigned with the Holder.

The "personal checking account signature form" which Best signed when the checking account was opened contained the following language:

> Should Bank receive any process, summons, order, injunction, execution, distraint, levy, lien, or notice, "Process," which in Bank's opinion affects this deposit, Bank may, at its option and without liability, thereupon refuse to honor orders to pay or withdraw sums from this account and may either hold the balance herein until Process is disposed of to Bank's satisfaction, or pay the balance over to the source of the Process.

* * * * * *

To secure any and all indebtedness and liability of (either or both) Depositors to Bank, however and whenever incurred or evidenced, whether direct or indirect, absolute or contingent, due, or to become due, Depositors (jointly and severally) hereby transfer and convey to Bank all balances, credits, deposits, monies and items now or hereafter in this account and Bank is authorized at any time to charge such indebtedness or liability against this account, whether or not the same is then due, and Bank shall not be liable for dishonoring items where the making of such a charge results in there being insufficient funds in this account to honor such items.

The district court held that under Georgia law the relationship of a depositor to a bank is one of creditor and debtor and that funds which are deposited are transformed into a chose in action. The district Court further held that in Georgia a chose in action is property or rights to property within the meaning of 26 U.S.C. § 6321. However, the court entered judgment for the bank upon finding that, under Georgia law, the language quoted herein from the promissory note constituted an assignment of Best's chose in action as collateral security for the debts evidenced by these promissory notes and operated as a valid assignment of all Best's rights as creditor of the Bank, existing by reason of his deposits, until the notes were paid. **See Macon National Bank v. Smith,** 170 Ga. 332, 338, 153 S.E. 4 (1930). Thus, C & S was not in possession of property or rights to property of the taxpayer at the time it received notice of the tax levy. For this reason, it cannot be held liable under section 6332(c) for its failure to turn over the funds

deposited in Best's account.

In a footnote the district court quoted the assignment language from the signature form and stated that it granted "similar contract rights" to the bank.

The taxpayer in No. 3571 is B&G Wrecker (B&G) which borrowed from the bank and opened a checking account on March 20, 1968. The collateral installment note which B&G executed provided that

> . . . the Holder may, at any time, without demand or notice of any kind, appropriate and apply toward the payment of such of the Libilities, and in such order of application, as the Holder may from time to time elect, any balances, credits, deposits, accounts, items or monies of the undersigned with the Holder.

B&G also executed a "deposit agreement" which contained language substantially identical to that quoted from the personal checking account signature form in No. 2549. In addition B&G gave the bank other collateral for the loan.

On June 10, 1969 IRS made an assessment of taxes against B&G and on June 13th a tax lien was filed in the proper recorder's office. On June 23, 1969 a notice of levy with respect to the B&G account was served on the bank. Immediately thereafter the bank made a setoff, crediting the B&G note for the full amount of the balance then carried in its account.

The district court held that under Georgia law when a person makes a general deposit in a bank, title to the money immediately passes to the bank and "the depositor simply has a claim against the Bank, which

claim is not considered 'property' or a 'right to property.' The court further held that since B&G's indebtedness to the bank was greater than the sum on deposit at the time of the levy "B&G had no claim of any nature which it could have successfully asserted against the Bank . . .." Relying on **United States v. Bank of Shelby,** 68 F.2d 538 (5th Cir. 1934), the district court stated,

> . . . since the Government's lien rights are derivative of those of the depositor, the Government takes subject to the defenses and equities affecting the depositor, so that even if the depositor has a claim, if it is not a claim which could have been maintained successfully by him, the Government is in no better position.

The court reasoned that the bank had both common law and statutory rights of setoff "and further, that this set-off could be made by the Bank either before it had knowledge of the Government's tax lien or after it became aware of it." The court concluded that the bank had "a contractual lien and security interest in the deposit which was created by the instruments taken by the Bank at the time the account was opened by the depositor." The district court found that the quoted language in the deposit agreement was a "specific transfer and conveyance of bank deposits as security for the loan by the Bank to B&G."

Our approach to the issues raised by these appeals has been chartered by the Supreme Court. In **Acquilino v. United States,** 363 U.S. 509, 512-14, 80 S.Ct. 1277, 1280, 4 L.Ed.2d 1365 (1960), the Court wrote:

> The threshold question in this case, as in all cases where the Federal Government asserts its tax lien, is whether and to what extent the tax-

payer had "property" or "rights to property" to which the tax lien could attach. In aswering that question, both federal and state courts must look to state law, for it has long been the rule that "in the application of a federal revenue act, state law controls in determining the nature of the legal interest which the taxpayer had in the property . . . sought to be reached by the statute." **Morgan v. Commissioner,** 309 U.S. 78, 82, 60 S.Ct. 424, 426, 84 L.Ed. 585. Thus, as we held only two Terms ago, Section 3670 "creates no property rights but merely attaches consequences, federally defined, to rights created under state law. . . ." **United States v. Bess,** 357 U.S. 51, 55, 78 S.Ct. 1054, 1057, 2 L.Ed.2d 1135. However, once the tax lien has attached to the taxpayer's state-created interests, we enter the province of federal law, which we have consistently held determines the priority of competing liens asserted against the taxpayer's "property" or "rights to property." (footnotes and citations omitted).

Thus we look first to the law of Georgia to determine whether Best and B&G had property or rights to property in their respective bank accounts at the time the government claims its tax liens attached.

[1] It is settled law in Georgia that a person who places money in a bank on general deposit loses title to the money and becomes a creditor of the bank. **McGregor v. Battle,** 128 Ga. 577, 58 S.E. 28, 29 (1907). The funds which are deposited are transformed into a chose in action. **Macon National Bank v. Smith,** 170 Ga. 332, 153 S.E. 4, 6-7 (1930); **Ricks v. Broyles,** 78 Ga. 610, 3 S.E. 772, 773 (1887). This court stated in **Broday v.**

United States, 455 F.2d 1097, 1099 (1972), ". . . once it has been determined under state law that the taxpayer owns property or rights to property, federal law is controlling for the purpose of determining whether a lien will attach to such property or rights to property." (citation omitted). Thus, having determined that a depositor in a Georgia bank is vested with a chose in action, we look to federal law to determine whether a chose in action is property or rights to property under §§ 6321 and 6331. In **United States v. Hubbeli,** 323 F.2d 197, 200 (5th Cir. 1963), after noting that "State law controls in determining the nature of the legal interest . . ." of one against whom a tax lien is asserted, ". . . but federal law controls the consequences attaching thereto . . . ," the court held that a chose in action is subject to levy as "property" or "right to property." **See also United States v. Metropolitan Life Insurance Co.,** 130 F.2d 149 (2d Cir. 1942); **United States v. Cohen,** 271 F.Supp. 709 (S.D.Fla.1967).

The bank in No. 2549 argues that the levy in that case was ineffective because (1) Best had conveyed to the bank "a security interest in his legal and equitable rights to the funds on deposit," (2) that feeling itself insecure, the bank had determined to apply Best's balance against his indebtedness prior to the service of notice of levy and had effective control over the Best account until appropriate entries could be made and (3) that even if Best had property or rights to property, the security interest of the bank was superior to the government lien. Principal reliance is placed on **Macon National Bank v. Smith,** supra, and **Georgia Bank & Trust Co. v. Hadarits,** 221 Ga. 125, 143 S.E.2d 627 (1965). In No. 3571 the chief argument of the bank is that where there are mutual debts between parties the claim of a delinquent debtor who owes more than he is owed is extinguished. Thus it is

contended that B&G had no interest in the balance on deposit in its account, because the larger claim of the bank against him left him with no enforceable claim against the bank. **Meriwether v. Bird,** 9 Ga. 594 (1851), **Skrine v. Simmons,** 36 Ga. 402 (1861), and **Taylor v. Jordan,** 57 Ga.App. 285, 195 S.E. 215 (1938), are cited in support of this position.

Although the Supreme Court of Georgia held in **Macon National Bank,** supra, that a bank depositor retains a chose in action, it further found that the chose in action had been assigned to the bank as collateral for a debt which exceeded the balance on deposit. The bank as transferee was held entitled to a "preference" with respect to the balance in the depositor's account as against the claim of a creditor who served a garnishment subsequent to the assignment. In **Georgia Bank & Trust Co. v. Hadarits,** supra, a bank to which a depositor had assigned all balances in his account as security for a note was held to have been "invested with a lien" upon all deposits of the maker of the note. The court further held that the bank did not receive a new benefit when it set off the depositor's account against his note and that the right of setoff was not lost by the payment of other checks drawn on the account after the assignment to the bank took place.

[2] The question of whether an assignment which is written to operate in the future divests the assignor of all rights in the property assigned has been answered differently by various courts, depending on the circumstances and applicable state law. **Compare United States v. Trigg,** 465 F.2d 1264 (8th Cir. 1972), **cert. denied,** 410 U.S. 909, 93 S.Ct. 963, 35 L.Ed.2d 270 (1973), **with Monroe Banking & Trust Co. v. Allen,** 286 F.Supp. 201 (N.D.Miss.1968). The statements in the opinions of the Supreme Court of Georgia that the

assignee banks are entitled to a "preference" or have a "lien" on the borrower's account are inconsistent with the arguments of the banks in this case that after the assignments the borrower-depositors had no property interests in their accounts. It would be anomalous to hold one entitled to a preference with respect to, or a lien upon, property of which he was the sole and absolute owner. The alternative finding of the district court in No. 3571 that "the Bank in this case had a contractual lien and security interest in the deposit . . ." is likewise inconsistent with the court's finding that the assignment from the depositor to the bank divested B&G of all property and rights to property in the deposit. If the bank was the sole owner of the deposit, it could not have a lien or security interest in it. If indeed the assignments created only rights to a preference or liens, then some property or rights to property remained in the depositors and the issue between the parties is one of priority of liens. However, the claim of a prior lien may not be interposed as a defense to an action to enforce a tax levy. **Commonwealth Bank v. United States,** 115 F.2d 327 (6th Cir. 1940); **United States v. Trans-World Bank,** 382 F.Supp. 1100, 1105 (C.D.Cal.1974). The banks may litigate the priority of liens issue in an action under 26 U.S.C. § 7426. Federal law is applied in determining property and such considerations as the chronology of the various steps taken by each of the parties and the "choateness' of the assignments are relevant. **See United States v. Pioneer American Insurance Co.,** 374 U.S. 84, 87, 83 S.Ct. 1651, 10 L.Ed.2d 770 (1963); **Hammes v. Tucson Newspapers, Inc.** 324 F.2d 101, 103 (9th Cir. 1963).

[3] Aside from the assignments the banks contend they were entitled to the benefit of a setoff of the balances in the Best and B&G accounts against the indebtedness

of each depositor. An examination of the provisions of the notes relating to setoff reveals that they speak of some positive act by the banks to effect setoff. In both instances the notes provide "the Holder may . . . appropriate and apply" the balances, credits, deposits and accounts of the borrower to his indebtedness. In No. 2549 the bank did not attempt to apply the Best balance to his debts until May 4, 1973, the day following service of notice of levy. In No. 3571 the setoff was made "immediately after" the notice of levy was served. Since the contractual right of setoff required some discrete act by the banks and neither bank in the present cases performed such an act until after service of notice of the levy, the depositors retained property interests in the accounts subject to levy, unless these interests had been extinguished by operation of law.

We again look to state law to determine whether the existence of an indebtedness to the bank which exceeds the balance in a depositor's account divests that depositor all property and rights to property in the account. Whatever may be the law in other states, [2] the law of Georgia does not seem to provide for an automatic setoff between bank and depositor. In **Taylor v. Jordan,** 57 Ga. App. 285, 195 S.E. 215, 216 (1938), the court stated that "[m]utual demands extinguish each other by operation of law, without waiting for any act of the parties." Neither the **Taylor** case nor the two older Georgia cases cited in the briefs involved mutual debts of

2. See United States v. National Bank of Commerce, 246 F.Supp. 597 (E.D.La.1965), for discussion of the statutory provision for "compensation." **But see United States v. First National Bank of Commerce** (No. 72-247, E.D.La. 1973), **aff'd per curiam,** 493 F.2d 1228 (5th Cir. 1974).

a bank and its depositor who was permitted to withdraw from his account after the mutual obligations came into existence. No Georgia case has been found which holds that a setoff by operation of law occurs where indebtedness of a bank depositor exceeds the balance of his deposits. On the other hand, Georgia cases involving the right of banks to set off debts against depositors' accounts uniformly indicate the requirement of some positive act. **E. g.,** "The bank's **action** . . ." (**Hadarits,** supra, 143 S.E.2d at 629); "When a bank which holds a note against one of its depositors **charges it up . . .**" (**Davenport v. State Banking Co.,** 126 Ga. 136, 54 S.E. 977 (1906)); ". . . having **exercised** this right . . ." [to set off] (**Caye v. Milledgeville Banking Co.,** 91 Ga. App. 664, 86 S.E.2d 717 (1955)). (emphasis added in each quotation). Moreover, the Uniform Commercial Code provision for setoff by banks, effective in Georgia since 1962, uses language connoting the necessity for some positive act on the part of the bank. "Any . . , setoff **exercised** by a payor bank . . ." (emphasis added) Ga.Code § 109A-4-303(1). **Compare Baker v. National City Bank of Cleveland,** 511 F.2d 1016 (6th Cir. 1975).

In **United States v. First National Bank of Arizona,** 348 F.Supp. 388, 389 (D.Ariz.1970), **aff'd per curiam,** 458 F.2d 513 (9th Cir. 1972), the District Judge wrote—

> Until a bank has notified its depositor and then **exercised** its right of setoff, the depositor is free to withdraw from his account and it is inconceivable that Congress, by virtue of 26 U.S.C. § 6323, intended to prohibit the Government from levying on that which is plainly accessible to the delinquent taxpayer-depositor. (emphasis in original).

A similar view was expressed by the Second Circuit in **United States v. Sterling National Bank & Trust Co. of N.Y.,** 494 F.2d 919, 921-22 (1974).

We do not believe that **United States v. Bank of Shelby,** 68 F.2d 538 (5th Cir. 1934), relied on by the banks in the present case leads to a contrary conclusion. In **Bank of Shelby** the depositor was insolvent and the bank account upon which the government sought to levy constituted the balance of proceeds of the very loan which the bank offset. The court held that ". . . where the mutual obligations have grown out of the same transaction, insolvency on the one hand justifies the set-off of the debt due upon the other" (quoting from **Scott v. Armstrong,** 146 U.S. 499, 507, 13 S.Ct. 148, 36 L.Ed. 1059 (1892)). **Id.** at 539.

We conclude that the government was entitled to judgments enforcing its levies in both cases before us because Best and B&G had property or rights to property in their respective bank accounts. As has been noted, both banks have argued that even if the depositors had property or rights to property in the accounts upon which levies were made, the banks had liens thereon which were superior to those of the government. The priority of liens is not before the court and we express no views on this issue.

[4] In No. 2549 the government sought a 50 per cent penalty as provided in 26 U.S.C. § 6332(c)(2) for failure of the bank to surrender property of the taxpayer "without reasonable cause." The district court did not reach this issue, but we conclude that there was a bona fide dispute as to whether the deposit represented property or rights to property of Best and that the penalty provision is not applicable in this case.

The judgment in each case is reversed and the cases are remanded to the district courts for entry of judgments for the government.

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 75-2549

D. C. Docket No. CA 174-51

UNITED STATES OF AMERICA,
Plaintiff-Appellant,

versus

CITIZENS AND SOUTHERN NATIONAL BANK,
Defendant-Appellee.

Appeals from the United States District Court for the Southern District of Georgia
Before WISDOM, GODBOLD and LIVELY*,
Circuit Judges.

JUDGMENT

This cause came on to be heard on the transcript of the record from the United States District Court for the Southern District of Georgia, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, reversed; and that this cause be, and the same is

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* Of the Sixth Circuit, sitting by designation.

hereby remanded to the said District Court in accordance with the opinion of this Court;

It is further ordered that defendant-appellee pay to plaintiff-appellant, the costs on appeal to be taxed by the Clerk of this Court.

September 15, 1976

Issued as Mandate:

United States Court of Appeals
FIFTH CIRCUIT

EDWARD W. WADSWORTH
CLERK

OFFICE OF THE CLERK

TEL. 504-589-6514
600 CAMP STREET
NEW ORLEANS, LA. 70130

November 16, 1976

TO ALL COUNSEL OF RECORD

NOS. 75-2549 & 75-3571 - USA v. Citizens and Southern National Bank

Dear Counsel:

This is to advise that an order has this day been entered denying the petition( ) for rehearing, and no member of the panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure; Local Fifth Circuit Rule 12) the petition( ) for rehearing en banc has also been denied.

See Rule 41, Federal Rules of Appellate Procedure for issuance and stay of the mandate.

Very truly yours,

EDWARD W. WADSWORTH, Clerk

By Susan M. Guevara
Deputy Clerk

/smg

cc: Mr. John D. Carey
Mr. Scott P. Crampton
Mr. Gilbert E. Andrews
Mr. E. S. Sell, Jr.
Mr. Charles T. Zink
Mr. Edmund A. Booth, Jr.
Mr. William M. Fulcher

United States Court of Appeals

FIFTH CIRCUIT

EDWARD W. WADSWORTH
CLERK

OFFICE OF THE CLERK

600 CAMP STREET
NEW ORLEANS, LA. 70130

December 2, 1976

Mr. William M. Fulcher
Attorney at Law
P. O. Box 1484
Augusta, GA 30903

No. 75-2549 - U.S.A. v. Citizens & Southern National Bank

MANDATE STAYED TO AND INCLUDING January 3, 1977

Dear Counsel:

The court has this day granted a stay of the issuance of the mandate to the date as shown above. If during the period of the stay there is filed with the clerk of this court a notice from the clerk of the Supreme Court that the party who has obtained the stay has filed a petition for the writ in that court, the stay shall continue until final disposition by the Supreme Court. Upon the filing of a copy of an order of the Supreme Court denying the petition for writ of certiorari the mandate shall issue immediately under Rule 41, FRAP.

Under revised Rule 21(1) of the Supreme Court effective July 1, 1970, a record is no longer required in connection with an application for writ of certiorari, and therefore will not be routinely prepared by this office (38LW 3502).

A copy of the opinion, judgment and denial of rehearing are still required by the Supreme Court to be incorporated as an appendix to your petition. Enclosed are copies of the said documents which have been entered in this cause.

Very truly yours,

EDWARD W. WADSWORTH, Clerk

By Mary Beth Breaux
Deputy Clerk

enc.

cc: Mr. Charles T. Zink
Mr. McChesney H. Jeffries
Mr. Scott P. Crampton
Mr. R. Jackson Smith, Jr.
Mr. Edmund A. Booth, Jr.

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

United States of America, Plaintiff	X	**Civil Action No. 174-51**
VS.	X	
Citizens and Southern National Bank, Defendant	X	

U. S. DISTRICT COURT
Southern District of Ga.
Filed in office
1:29 P.M.
April 21, 1975
/s/ P. A. Brodie
Deputy Clerk

ORDER

This case involves a dispute relating to the obligations of the defendant Bank as the result of a tax levy affecting R. W. Best, one of its depositors. Plaintiff, United States of America, asks this Court to declare defendant, Citizens and Southern National Bank (C & S), personally liable pursuant to 26 U.S.C. § 6332 (c) (1) for its refusal to honor an Internal Revenue Service levy served upon it on May 3, 1973. Additionally, the Government seeks to impose a penalty equal to fifty percent (50%) of the amount recoverable by virtue of the levy on the Bank under 26 U.S.C. § 6332 (c) (2) for its alleged failure to act with "reasonable cause" in refusing to honor the levy. The case is now before the Court on the parties' stipulations of material facts.

On May 2, 1973, the Government made an income tax assessment and demand for payment against Robert W. Best for unpaid wagering excise taxes in the amount of $741,093.49 for the taxable period commencing January 1, 1969, and terminating November 30, 1972. Notwithstanding notice and demand, Best failed and refused to pay the assessment. Notice of federal tax liens for the assessment was then filed in the office of the Clerk of the Superior Court of Richmond County, Georgia, and on May 3, 1973, at 3:05 P.M., Internal Revenue Service agent W. B. Hayes served a notice of levy on C & S directing it to remit to the I.R.S. all of Best's property in account number 001-59-509, which at the time of the service of notice contained $57,365.58.

Prior to this time during 1972 and 1973, Best had borrowed money in excess of $60,000.00 from C & S, as evidenced by six promissory notes executed or endorsed by Best alone of by Best and George C. Nicholson. [1] See Stipulation Exhibits 16-20. Under the terms of the notes, Best gave C & S a continuing security interest and right of set-off upon "any and all balances, credits, deposits,

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[1] Two of the notes, numbers 92753 and 90759, were merely endorsed by Best and Nicholson. See Stipulation Exhibits 18 and 20. Number 92753 was executed by J. B. Palmer, Jr., in the amount of $15,000.00 and number 90759 was executed by Columbia Road Builders in the amount of $20,000.00. The amount which Best owed C & S under promissory notes executed by himself alone or by himself and George Nicholson exceeded $60,000.00. Consequently, this Court need not consider whether the Bank's alleged contractual right of set-off extended to obligations Best assumed as a mere guarantor or whether it applied only to notes under which Best was obligated either as a maker or co-maker. See, e.q., Chandler v. Bank of Waynesboro, 29 Ga. App. 5, 6 (1922); 13 ENCYCLOPEDIA OF GEORGIA LAW, Guaranty and Suretyship § 22.

accounts, items and monies" Best maintained with C & S to be applied against any and all indebtedness, whether matured or unmatured. Id.

On May 3, 1973, the date when the Government filed notice of a lien on Best's account, the Finance Committee of the C & S Bank determined at its 12 noon meeting that it was insecure [2] as to the debts owed by Best as maker, co-maker or endorser, and that it would appropriate and apply Best's balance on deposit and debit his accounts against amounts owed by him to the Bank. At this time, the Executive Branch of the Bank, represented by Mr. Emory Lewis, who was employed by C & S as Vice President and Senior Commercial Loan Officer during 1973, regarded Best's account as under the control of the Bank, and apparently would have restricted any substantial withdrawal from his accounts. However, it was not until May 8, 1973, that C & S actually charged Best's indebtedness against his accounts and appropriated and applied the balances to the amounts owed. Accordingly, the Bank did not remit the funds in the taxpayer's account as the notice of levy had instructed.

After C & S notified Revenue Officer Hayes by letters dated May 8, 1973, and May 17, 1973, that it had applied the balance of account number 001-59-509 to Best's outstanding obligations with the Bank, the Government made final demand upon William Brigham, Vice-

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[2] The Bank deemed itself insecure as a result of Best's indictment on April 30, 1973, by a federal grand jury for participation in certain illegal gambling operations. The indictments resulted from raids conducted by federal and state law enforcement officers on November 10, 1972, in and about Augusta, Georgia, and related investigations.

President of C & S on November 19, 1973, at 3:45 P.M. See Stipulation Exhibits 33-35. Following the Bank's continuing refusal to honor the Government's levy, this action was initiated on May 16, 1974.

Section 6332 (c) (1) [3] provides that a person refusing to honor a tax levy is personally liable to the United States for the value of the taxpayer's property or right to property not surrendered. Moreover, under section 6332 (c) (2) [4] a person failing to surrender property belonging to the taxpayer "without reasonable cause" will be liable for a penalty "equal to 50 percent of the amount recoverable" under section 6332 (c) (1). The amount sued for by the Government and claimed as the amount recoverable is $57,365.58, together with a penalty equal to half this amount, interest, and costs.

It is well-settled that the only defenses to a levy on the

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[3] 26 U.S.C. § 6332 (c) (1) provides: "Any person who fails or refuses to surrender any property or rights to property, subject to levy, upon demand by the Secretary or his delegate, shall be liable in his own person and estate to the United States in a sum equal to the value of the property or rights not so surrendered, but not exceeding the amount of taxes for the collection of which such levy has been made, together with costs and interest on such sum at the rate of 6 percent per annum from the date of such levy. Any amount (other than costs) recovered under this paragraph shall be credited against the tax liability for the collection of which such levy was made."

[4] 26 U.S.C. § 6332 (c) (2) provides: "In addition to the personal liability imposed by paragraph (1), if any person required to surrender property or rights to property fails or refuses to surrender such property or rights to property without reasonable case, such person shall be liable for a penalty equal to 50 percent of the amount recoverable under paragraph (1). No part of such penalty shall be credited against the tax liability for the collection of which such levy was made."

taxpayer's debtor issued pursuant to 26 U.S.C. § 6321 [5] are first, that the person levied upon had no property or rights to property of the taxpayer in his possession at the time of the levy; and second, that such property or rights to property then held were subject to attachment or other judicial process. **E.q., United States v. Manufacturers Trust Co.,** 198 F.2d 366, 369 (2d Cir. 1952); **United States v. Transworld Bank,** 74-2 U.S.T.C. 9632, 9637 (C.D. Calif. 1974); **United States v. Sterling Bank & Trust Co.,** 360 F. Supp. 917, 923 (S.D. N.Y. 1973), **aff'd in relevant part,** 494 F.2d 919, 921 (2d Cir. 1974). Therefore, the defense of lien priority is not applicable in a suit brought to enforce a tax levy under this section. Furthermore, in the present case, there is no contention that Best's property was subject to attachment or other judicial process. Thus, the only issue which this Court must consider is whether the defendant had property or rights to property of the taxpayer in his possession at the time of the levy. This question must be determined by looking at state law. **Acquilino v. United States,** 363 U.S. 509 (1960); **See United States v. Bank of Commerce,** 73-2 U.S.T.C. 9751 (E.D. La. 1973), **aff'd per curiam,** 34 A.F.T.R. 2d 74-5056 (5th Cir. 1974).

In Georgia, a general deposit of funds in a bank ordinarily creates the relationship of debtor and creditor between the bank and its depositor. **E.q., McGregor v. Battle,** 128 Ga. 577 (1907). In the absence of some

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[5] 26 U.S.C. § 6321 states: "If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person."

agreement to the contrary, legal title to money deposited in a bank immediately passes to the bank, and the credit of the bank is substituted for the money. **Id.; Davenport v. State Banking Co.,** 126 Ga. 136 (1906). Thus, "(a) general deposit is a loan, and transforms the funds from ready money into a chose in action." **E.q., Macon National Bank v. Smith,** 170 Ga. 332, 337 (1930), **quoting with approval, Ricks v. Broyles,** 78 Ga. 610(4) (1887).

Generally, a chose in action or right to bring suit constitutes the property of the person to whom the right of action runs. **E.q., Maryland Casualty Co. v. Brown,** 321 F. Supp. 309, 311 (N.D. Ga. 1971); **See Sterling v. Sims,** 72 Ga. 51 (1883). Consequently, the Court of Appeals for the Fifth Circuit has held that in Georgia a chose in action is property or rights to property within the meaning of 26 U.S.C. § 6321, giving the Government a lien on all the property of a taxpayer who fails to pay his taxes following demand. **United States v. Hubbell,** 323 F.2d 197, 200 (5th Cir. 1963). On the basis of these cases the Government contends in this case that even assuming C & S had a right of set off against Best's account, the fact that Best had a property right in his account prior to the time the Bank actually exercised its right of set off obligated the bank to honor the tax levy.

Whatever the merits of the Government's position with respect to any common law right of set off the Bank may have possessed, this Court is of the opinion that under the rationale of **Macon National Bank v. Smith,** 170 Ga. 332 (1930), [6] the critical factor in this case is not

[6] The Georgia Supreme Court has cited **Macon Nat'l Bank v. Smith,** 170 Ga. 332 (1930) approvingly in more recent cases. **E.q., Georgia Bank & Trust Co. v. Hadarits,** 221 Ga. 125, 128 (1965); **Backer v. City Bank & Trust Co.,** 180 Ga. 672, 673 (1935).

whether the Bank actually exercised its right of set off at the time of the levy, but whether Best gave C & S a security interest in his deposits at the time he borrowed money from the Bank. "In **Macon National Bank v. Smith, supra,** the Georgia Supreme Court held that when deposits of a debtor are given as collateral security for promissory notes executed in favor of a bank, the Bank has a valid assignment of the debtor's chose in action. 170 Ga. at 337-39. Thus, a debtor's legal and equitable rights to his funds on deposit with a bank terminate at the date the promissory notes assigning his deposits as collateral security are executed. **Id.** at 338-39; **See Georgia Bank & Trust Co. v. Hadarits,** 221 Ga. 125 (1965); **Backer v. City Bank & Trust Co.,** 180 Ga. 672 (1935)." As a result, a taxpayer has no property or right to property in deposits he makes with a bank possessing a security interest in his accounts.

Here, Best executed promissory notes in excess of $57,365.58, all of which contained the following provision:

> "To secure the payment of this Note and all other indebtedness or liabilities of the undersigned to holder, however and whenever incurred or evidenced, whether direct or indirect, absolute or contingent, or due or to become due . . . . undersigned transfers and conveys to Holder any and all balances, credits, deposits, accounts, items and monies of the undersigned now or hereafter with the Holder, and the undersigned "agrees that the Holder shall have a lien upon, security title to and a security interest in all property of the undersigned of every kind and description now or hereafter in the possession or control of the Holder for any reason . . . ." **See** Stipulation Exhibits 16-20.

Under Georgia law, this clause constituted an assignment of Best's chose in action as collateral security for the debts evidenced by these promissory notes and operated as a valid assignment of all Best's rights as creditor of the Bank, existing by reason of his deposits, until the notes were paid. **See Macon National Bank v. Smith,** 170 Ga. 332, 338 (1930). Thus, C & S was not in possession of property or rights to property of the taxpayer at the time it received notice of the tax levy. For this reason, it cannot be held liable under section 6332(c) for its failure to turn over the funds deposited in Best's account. [7]

Accordingly, judgment is hereby entered in favor of the defendant.[8]

So Ordered, this 21st day of April, 1975.

/s/ Anthony A. Alaimo
United States District Judge

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[7] Similar contract rights were granted by Best to C & S when Best opened account number 001-59-509: "To secure any and all indebtedness and liability of (either or both) Depositors to Bank, however, and whenever incurred or evidenced, whether direct or indirect, absolute or contingent, due, or to become due, Depositors (jointly and severally) hereby transfer and convey to Bank all balances, credits, deposits, monies and items now or hereafter in this account and Bank is authorized at any time to discharge such indebtedness or liability against this account whether or not the same is then due, and Bank shall not be liable for dishonoring items where the making of such a charge results in there being insufficient funds in this account to honor such items." Stipulation Exhibit 1.

[8] In deciding in favor of the defendant, this Court does not reach the question of whether the Bank's contractual right of set off

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8 (cont'd.)

constituted a security interest within the meaning of 26 U.S.C. § 6323 (a) providing that if the third party lienor becomes "holder of a security interest" before the tax lien is publicly filed, the third party has a priority over the tax lien. Rather, the basis for this decision is solely that since the defendant was not in possession of Best's property at the time of the levy, the levy could not operate to divest the Bank of the taxpayer's property.

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

United States of America, **Plaintiff**	X	**Civil Action No. 174-51**
vs.	X	
Citizens and Southern National Bank, **Defendant**	X	

U. S. DISTRICT COURT
Southern District of Ga.
Filed in office
1:15 p.m.
August 22, 1975
/s/ P. A. Brodie
Deputy Clerk

FINAL JUDGMENT

Upon the Order of this Court entered April 21, 1975, determining that plaintiff is not entitled to recover of the defendant, judgment is hereby entered in favor of the defendant, and

IT IS CONSIDERED, ORDERED, AND ADJUDGED that plaintiff take nothing and the case stands dismissed.

This 22nd day of August, 1975.

/s/ Anthony A. Alaimo
United States District Judge

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 6321. LIEN FOR TAXES.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

SEC. 6323 [as amended by Sec. 101 (a), Federal Tax Lien Act of 1966, supra].

(a) **Purchases [Purchasers], Holders of Security Interests, Mechanic's Lienors, and Judgment Lien Creditors.** --The lien imposed by section 6321 shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice thereof which meets the requirements of subsection (f) has been filed by the Secretary or his delegate.

(h) **Definitions.**--For purposes of this section and section 6324--

(1) **Security interest.**--The term "security interest" means any interest in property acquired by contract for the purpose of securing payment or performance of an obligation or indemnifying against loss or liability. A security interest exists at any time (A) if, at such time, the property is in existence and the interest has become protected under local law against a subsequent judgment lien arising out of an unsecured obligation, and (B)

to the extent that, at such time, the holder has parted with money or money's worth.

SEC. 6331. Levy and distraint

(a) Authority of Secretary or delegate.—If any person liable to pay any tax neglects or refuses to pay the same within 10 days after notice and demand, it shall be lawful for the Secretary or his delegate to collect such tax (and such further sum as shall be sufficient to cover the expenses of the levy) by levy upon all property and rights to property (except such property as is exempt under section 6334) belonging to such person or on which there is a lien provided in this chapter for the payment of such tax. Levy may be made upon the accrued salary or wages of any officer, employee, or elected official, of the United States, the District of Columbia, or any agency or instrumentality of the United States or the District of Columbia, by serving a notice of levy on the employer (as defined in section 3401(d)) of such officer, employee, or elected official. If the Secretary or his delegate makes a finding that the collection of such tax is in jeopardy, notice and demand for immediate payment of such tax may be made by the Secretary or his delegate and, upon failure or refusal to pay such tax, collection thereof by levy shall be lawful without regard to the 10-day period provided in this section.

(b) Seizure and sale of property.—The term "levy" as used in this title includes the power of distraint and seizure by any means. A levy shall extend only to property possessed and obligations existing at the time thereof. In any case in which the Secretary or his delegate may levy upon property or rights to property, he may seize and sell such property or rights to property (whether real or personal, tangible or intangible).

SEC. 6332. Surrender of property subject to levy

(a) Requirement.—Except as otherwise provided in subsection (b), any person in possession of (or obligated with respect to) property or rights to property subject to levy upon which a levy has been made shall, upon demand of the Secretary or his delegate, surrender such property or rights (or discharge such obligation) to the Secretary or his delegate, except such part of the property or rights as is, at the time of such demand, subject to an attachment or execution under any judicial process.

(c) Enforcement of levy.—

(1) Extent of personal liability.—Any person who fails or refuses to surrender any property or rights to property, subject to levy, upon demand by the Secretary or his delegate, shall be liable in his own person and estate to the United States in a sum equal to the value of the property or rights not so surrendered, but not exceeding the amount of taxes for the collection of which such levy has been made, together with costs and interest on such sum at the rate of 6 percent per annum from the date of such levy. Any amount (other than costs) recovered under this paragraph shall be credited against the tax liability for the collection of which such levy was made.